



OFFICE OF
CHIEF COUNSEL

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

CC:EBEO:Br.4:EMadden
FREV-108458-99
JUL - 6 1999

MEMORANDUM FOR DIRECTOR, EMPLOYEE PLANS DIVISION (EP/EO)
Attention: Ann Trichilo

FROM: Assistant Chief Counsel (Employee Benefits and Exempt
Organizations), CC:EBEO

SUBJECT: [REDACTED]

This memorandum responds to your memorandum dated April 28, 1999, requesting assistance regarding section 404 of the Internal Revenue Code.

LEGEND

Plan = [REDACTED]
EIN: [REDACTED]

Union = [REDACTED]
[REDACTED]

Employer = [REDACTED]
EIN: [REDACTED]

The relevant facts, as we understand them, are as follows. Members of Union presently participate in Plan, a multiemployer defined pension plan that is qualified under section 401(a) of the Code. The contribution rate to Plan is determined by a collective bargaining agreement.

An actuarial study of Plan indicates that pension benefits accrued by employees may be adversely affected by section 415 of the Code if the employees were to receive unreduced early retirement benefits at a relatively early age and that benefits for younger employees may also be adversely affected if they continue to work in the [REDACTED] business. In response to these projections, Plan trustees will create an Excess Benefit Plan to provide benefits that a Plan participant would have received under Plan in the absence of the annual benefit limitations imposed by section 415.

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The Excess Benefit Plan is designed to provide, on a nonqualified basis, benefits in excess of those permitted to be paid by Plan by reason of the limitations imposed by section 415 of the Code. The Excess Benefit Plan provides that a participant will receive payments from the Excess Benefit Plan each month equal to the amount by which the Excess Benefit Plan participant's monthly benefits from Plan, calculated under Plan's benefit formula (without taking into account the section 415 limits) exceeds the maximum benefit that Plan can pay to the participant without violating the section 415 limitations. The amount to be paid by the Excess Benefit Plan will be increased to reflect FICA taxes due thereon so that the benefit payment (net of FICA taxes) paid by the Excess Benefit Plan to the participant will be the same amount to which the Excess Benefit Plan participant would be entitled to had the excess benefit payment not been subject to FICA taxes. FICA taxes attributable to the Excess Benefit Plan payments will be remitted to the Service as required by the Code.

The Excess Benefit Plan is not expected to hold significant assets. Pursuant to the collective bargaining agreement, the amount of benefits to be paid by the Excess Benefit Plan in a given month plus FICA taxes and administrative expenses will be remitted to the administrative manager of the Excess Benefit Plan each month. The amount of benefits to be paid each month will be allocated to separate bookkeeping accounts for those participants who are entitled to receive benefits from the Excess Benefit Plan. The trust associated with the Excess Benefit Plan will merely act as a passthrough entity for excess benefit payments and related expenses. All amounts received by the Excess Benefit Plan, including trust income, will be allocated to the payment of the Excess Benefit Plan expenses and then to pay benefits to the Excess Benefit Plan participants each month. Benefit payments and expenses will be paid from the Excess Benefit Plan shortly after they are allocated and will be paid out before the end of each tax year. No principal amounts or interest income, if any, will be allowed to accumulate in the Excess Benefit Plan trust. The administrative manager of Plan will act as administrative manager of the Excess Benefit Plan.

To fund the Excess Benefit Plan, the collective bargaining agreement will be amended. This amendment will modify Plan funding as follows. First, the collective bargaining agreement will require the administrative manager of Plan to calculate, on a monthly basis, the amount necessary to pay the Excess Benefit Plan benefits and expenses for the month. Second, the collective bargaining agreement amendment will require the administrative manager of Plan to deduct the amount necessary to pay the Excess Benefit Plan benefits, FICA taxes, and related administrative expenses from the funds received from employers, including Employer. The amount necessary to pay the Excess Benefit Plan benefits and expenses will be transmitted to the Excess Benefit Plan for payment to the Excess

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Benefit Plan participants or for the payment of administrative expenses. Third, all contributions not remitted to the Excess Benefit Plan are then forwarded to Plan trust fund. Thus, Employer, as well as other employers of bargaining unit employees, will continue to submit the required employer contributions for each hour worked by each bargaining unit member to the administrative manager of Plan. However, pursuant to the terms of the collective bargaining agreement, a portion of the funds will be remitted to the Excess Benefit Plan and the remainder of the funds will be submitted to Plan.

Once payments are received by Plan, they cannot be shifted to the Excess Benefit Plan. Thus, the only contributions that will be allocated to the Excess Benefit Plan are those that are required to be allocated to the Excess Benefit Plan by the terms of the collective bargaining agreement. This allocation will always occur before the funds are deposited in any Plan account.

Plan requests a ruling, within our jurisdiction, that any employer contributions allocated to the Excess Benefit Plan pursuant to the collective bargaining agreement, if otherwise deductible, will be deductible by the employers under section 404 of the Code.

Assuming the above-described facts are included, we suggest the following be included in your response to Fund.

Section 404(a) of the Code provides the general deduction timing rules applicable to a stock bonus plan, pension, profit sharing, or annuity plan, or if compensation is paid or accrued on account of any employee under a plan or arrangement for deferring compensation, regardless of the Code section under which the amounts might otherwise be deductible. Pursuant to section 404(a)(5), contributions or compensation deferred under a nonqualified plan or arrangement, if otherwise deductible, are deductible in the taxable year in which an amount attributable to the contribution are includible in the gross income of the employees participating in the plan, but in the case of a plan in which more than one employee participates, only if separate accounts are maintained for each employee. See also section 1.404(a)-12(b)(3) of the Income Tax Regulations.

Section 1.404(a)-12(b)(3) of the regulations provides that a deduction is allowable for contributions paid only in the taxable year in which or with which ends the taxable year of an employee in which an amount attributable to the contribution is includible in his or her income as compensation, and then only to the extent allowable under section 404(a).

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Because employees who participate in the Excess Benefit Plan are fully vested in their benefits when employer contributions are made and separate accounts are maintained for each employee, each employer who participates in the Excess Benefit Plan is entitled to a deduction under section 404(a)(5) of the Code in an amount equal to the amount included in income by their respective employees, assuming all other requirements for deductibility are met. The deduction is allowable in the taxable year in which or with which ends the taxable year of the employee in which the amount is includible in the employee's income as compensation.

Accordingly, we rule as follows:

3. That any employer contributions allocated to the Excess Benefit Plan pursuant to the collective bargaining agreement, if otherwise deductible, will be deductible by the employers under section 404 of the Code.

Except as specifically ruled above, no opinion is expressed regarding the subject transaction under any other provision of the Code, including the consequences to participants under section 83 and 402(b) of the Code. Moreover, we express no opinion regarding the federal employment tax aspects of the above-described transaction.

If you have any questions regarding this memorandum, please contact Erinn Madden in my office at (202) 622-6060.

Mary Oppenheimer
Assistant Chief Counsel

By:



MARK SCHWIMMER
Chief, Branch 4
Office of the Associate Chief
Counsel (Employee Benefits and
Exempt Organizations)